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SUBJECT: EGYPTIAN QIZ'S IN JORDANIAN PERSPECTIVE

REF: CAIRO 846

Classified By: Ambassador Edward W. Gnehm, Reasons 1.5 (b,d)

1. (c) SUMMARY: Activating the QIZ initiative in Egypt through parallel protocols would have profound effects on the long-term viability of QIZ's in Jordan. More seriously, such a deal would cause deep concern within the GOJ about equitable treatment for the politically tough decisions Jordan has made with regard to normalizing relations with Israel. Especially at this sensitive time, we believe activation of Egyptian participation in the QIZ initiative should not be done in such a way as to expose the GOJ to strong domestic criticism for giving up more than it had to politically vis-a-vis Israel. End summary.

ECONOMIC IMPACT PREDICTABLY BAD

2. (c) We expect senior levels of the GOJ to react with dismay when news that Egypt is activating its QIZ option gets out. Economically, this is predictable, as full Egyptian participation in the QIZ initiative would severely curtail QIZ sales and new investment in Jordan. For example, the Vice President for Sourcing of Target, in a recent visit to Amman, told us that preferential access to the U.S. market along the lines of the QIZ initiative would make Egypt's vertically integrated textile industry a far more advantageous place to source from than Jordan, which lacks both the high-quality local cotton and the vertical integration.

3. (c) In addition to the impact on the nascent western-oriented business sector, diversion of QIZ business to Egypt would have severe repercussions on Jordan's balance of payments and the King's efforts to diversify the economy away from dependence on foreign aid, remittances, and exports to Iraq. The QIZ's were responsible for over \$400 million in gross hard currency inflows in 2002 (5% of GDP and 20% of total exports). Exports of \$600-800 million are possible this year, more than combined U.S. military and economic assistance. According to a recent study by the EU assistance mission, QIZ exports have the potential to reach \$2.6 billion annually as soon as 2007 -- under current conditions.

POLITICAL COSTS EVEN MORE DAMAGING

4. (c) More disturbing, though, is the major political embarrassment that Egypt's participation in the QIZ initiative on "easier" political terms could cause the GOJ. Should Egypt activate its QIZ participation in the same manner as the GOJ did, i.e. with an agreement between the GOE and the GOI, Jordan would have no real political exposure. If, however, the Egyptians use a parallel protocols mechanism (reftel), we expect the GOJ to register deep concern. The GOJ took brave political risks to initiate the QIZ's, invoking the ire of anti-normalization groups and provoking death threats against some of the early investors. Since then, the success of the initiative has quieted anti-normalization voices. In addition, in providing jobs to over 20,000 (primarily rural, conservative) Jordanians, the QIZ's have played an important role in changing public attitudes about working with Israel.

5. (c) All of these gains would be put at risk if Egypt was seen by the GOJ as getting an "easier deal" than Jordan received. The GOJ will perceive this as favoritism toward Egypt, obliging Jordan to make public and direct government-to-government ties to Israel, while Egypt is not asked to take similar risks. This analysis, irrespective of the economic impact of competition for QIZ sales and investment, would light a hitherto smoldering fire under the anti-normalizers. Worse, it would dissuade forward-leaning Jordanians from taking on new political risks vis-a-vis Israel, on the assumption that, if they wait long enough, they can get "Egyptian terms." It will also dissuade liberal Jordanian businessmen from reaching out to do business with Israel out of fear they could be undercut later on by more "favorable" treatment third countries receive. Finally, it will disappoint Jordanian workers (those that remain after

the economic effects reveal themselves), who will perceive Egyptian workers as getting the benefits of the QIZ's without having to work with Israel. Whether or not this is true would be irrelevant - the perception would be the same.

COMMENT

16. (c) While Egypt's long-overdue participation in the QIZ initiative will cause serious economic disruption to Jordan's nascent garment sector, this is a normal facet of the cut-throat global textile industry. Jordan has always known it would need to deal with competition from abroad, and should be expected to find ways to compensate for the disruption (re-training, diversification, etc). In any event, there will still be a niche for Jordanian garment exports: The inclusion of Egypt might even create new partnership opportunities among QIZ exporters, and Jordan will still be a good sourcing option for synthetic fabric-based garments, where Egyptian advantages in cotton and vertical integration are not as much in play. The GOJ's track record on QIZ investor support and on relations with Israeli counterparts could also be a distinct advantage.

17. (c) That said, bringing Egypt into the QIZ fold needs to be managed in such a way that it does not overturn the political sacrifices Jordan made. Preserving the momentum the QIZ's have generated in beating back the anti-normalization lobby means making sure that hard-won benefits are not given to other countries that have not been asked to make the same difficult decisions.
GNEHM